87-2032

Supreme Court, U.S.
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No.

IN THE
SUPREME COURT OF THE UNITED STATES

October Term, 1987

THOMAS E. LILLY,

Petitioner,

v.

EBSCO INDUSTRIES, INC.,

Respondent.

PETITION FOR A WRIT OF CERTIORARI
TO THE
UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

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QUESTIONS PRESENTED FOR REVIEW

1. Whether a federal district court may issue a preliminary injunction, prohibiting a defendant from spending his assets, in order to preserve a pool of funds for the payment of a potential future money judgment?

2. Whether a federal district court, under Fed. R. Civ. P. 64, may choose to ignore the requirements of the state prejudgment attachment statute and issue an order, under Fed. R. Civ. P. 65, freezing a defendant's assets in order to preserve those assets to satisfy a potential money judgment?

PARTIES

The caption of this petition contains the names of all parties to the proceeding in the court below. Petitioner Thomas E. Lilly is an individual.

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IN THE

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October Term, 1987

No. _____

THOMAS E. LILLY,

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v.

EBSCO INDUSTRIES, INC.,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

Thomas E. Lilly respectfully petitions for a writ of certiorari to review the order of the United States Court of Appeals for the Sixth Circuit entered in this case.

OPINIONS BELOW

The preliminary injunction order of the United States District Court for the Southern District of Ohio, which was entered on May 22, 1986, unreported, is attached as Appendix A. The same court's Findings of Fact and Conclusions of Law Supporting Issuance of Preliminary Injunction, also unreported, was entered on August 1, 1986 and is attached as Appendix B. The opinion of the United States Court of Appeals for the Sixth Circuit, and dissenting opinion, are attached as Appendix C and reported at 840 F.2d 333 (6th Cir. 1988).

JURISDICTION

The judgment of the Sixth Circuit was entered on February 23, 1988. This Court's jurisdiction over this petition exists pursuant to sections 1254 and 2101 of 28 United States Code.

STATUTES INVOLVED

Rule 64, Federal Rules of Civil Procedure

SEIZURE OF PERSON OR PROPERTY

At the commencement of and during the course of an action, all remedies providing for seizure of person or property for the purpose of securing satisfaction of the judgment ultimately to be entered in the action are available under the circumstances and in the manner provided by the law of the state in which the district court is held, existing at the time the remedy is sought, subject to the following qualifications: (1) any existing statue of the United States governs to the extent to which it is applicable; (2) the action in which any of the foregoing remedies is used shall be commenced and prosecuted or, if removed from a state court, shall be prosecuted after removal, pursuant to these rules. The remedies thus available include arrest, attachment, garnishment, replevin, sequestration, and other corresponding or equivalent remedies, however designated and regardless of whether by state procedure the remedy is ancillary to an action or must be obtained by an indpendent action.

Rule 65(a), Federal Rules of Civil Procedure

INJUNCTIONS

(a) Preliminary Injunction

(1) Notice. No preliminary injunction shall be issued without notice to the adverse party.

(2) Consolidation of Hearing With Trial on Merits. Before or after the commencement of the hearing of an application for a preliminary injunction, the court may order the trial of the action on the merits to be advanced and consolidated with the hearing of the application. Even when this consolidation is not ordered, any evidence received upon an application for a preliminary injunction which would be admissible upon the trial on the merits becomes part of the record on the trial and need not be repeated upon the trial. This subdivision (a)(2) shall be so construed and applied as to save to the parties any rights they may have to trial by jury.

Ohio Revised Code, Sections 2715.01(A), 2715.03 and 2715.044 of the Ohio Revised Code are reproduced in Appendix D.

STATEMENT OF THE CASE

(a) Facts

Respondent EBSCO Industries, Inc. ("EBSCO") commenced this action on April 18, 1986 by filing its complaint against Petitioner Thomas E. Lilly ("Lilly") in the United States District Court for the Southern District of Ohio. The sole jurisdictional basis alleged for the action was diversity of citizenship, 28 U.S.C. §1332.[1]

In this complaint for money damages EBSCO asserted state law claims of fraud and breach of contract arising out of EBSCO's 1983 purchase of some of the assets of Four Seasons Garment Corporation and also in connection with Lilly's subsequent service as general manager of

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[1]Citations to the record before the Court of Appeals are cited as "R. _____".

EBSCO's Four Seasons division.[2] At the time of this asset purchase by EBSCO in 1983, Lilly had been the chief executive officer and one of the major shareholders Four Seasons.

The gist of the complaint was that, at the time of this asset purchase, Lilly defrauded EBSCO by falsifying and overstating the accounts receivable of the Four Seasons corporation. However, EBSCO never purchased these accounts receivable.[3] EBSCO's relationship to these overstated accounts receivable was indirect. EBSCO claimed that the receivables were falsified and overstated in order to induce EBSCO, in 1983, to buy other assets of Four Seasons and to loan to the Four Seasons corporation almost $3 million to satisfy a pre-existing Four

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[2]R. 1: Complaint.

[3]R. 44: Transcript of Hearing, Exh. 1: Asset Purchase Agreement.

Seasons corporation debt to First National Bank of Boston (secured by those receivables).[4] EBSCO paid the bank loan and, in turn, was to be repaid by the Four Seasons corporation from the accounts receivable as they were collected.[5] This loan from EBSCO to the Four Seasons corporation was guaranteed by Lilly.[6]

EBSCO alleged that, after the EBSCO asset purchase from Four Seasons, Lilly and others continued to falsify and overstate the accounts receivable, preventing EBSCO from learning that there had not been enough actual receivables for the

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[4]R. 44: Transcript of Hrg, at 33.

[5]Lilly did not receive any loan proceeds; rather, EBSCO wired the money directly to the Boston bank, thereby paying the obligation of Four Seasons Garment Corporation to that bank. Id., Transcript of Hearing, at 35.

[6]R. 44: Transcript of Hearing, at Exh. 10-12.

Four Seasons corporation to repay the loan from EBSCO. In other words, EBSCO claimed that its loan was being repaid with receipts from post-acquisition receivables, i.e., its own money. EBSCO alleged that this scheme to overstate the accounts receivable was discovered on March 31, 1986 and that Lilly resigned on April 1, 1986.

(b) The Preliminary Injunction.

EBSCO's initial effort in this litigation was to attach or freeze all of Lilly's personal assets to preserve a pool of funds in case it obtained a money judgment against him. To that end, EBSCO sought an order from the district court to prevent Lilly from spending his own personal assets during the pendency of the litigation. EBSCO elected to ignore the relief available under Ohio's prejudgment

attachment statutes, Chapter 2715 of the Ohio Revised Code, through Fed. R. Civ. P. 64.[7] Instead, EBSCO filed a motion for a preliminary injunction, pursuant to Fed. R. Civ. P. 65, seeking an order prohibiting Lilly from spending his assets until a judgment was recovered.[8] EBSCO's own memorandum stated clearly its aim in moving for preliminary relief:

> Available financial information raises substantial questions about the collectibility of a judgment if [Lilly's] assets are not available at that time.[9]

At the hearing on EBSCO's motion for a preliminary injunction, the district court inquired as to why EBSCO was not pursuing, under Fed. R. Civ. P. 64, relief available under Ohio's prejudgment

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[7]Chapter 2715 of the Ohio Revised Code, contains Ohio's prejudgment attachment requirements.

[8]R. 10: Motion for Preliminary Injunction.

[9]Id., at 7.

attachment statutes.[10] EBSCO responded that it believed that the protective bond requirements which the Ohio legislature mandated in the statute were "unrealistic" and "not practical."[11] There was no evidence presented at the hearing that Lilly personally had ever received any funds belonging to EBSCO.

After the hearing on EBSCO's motion for preliminary injunction, the district court found all the requirements of Fed. R. Civ. P. 65 had been met, concluded that Lilly may try to transfer his assets, and issued a far-reaching injunction. See Appendix A. The injunction prohibits Lilly from using his personal property except "basic living expenses"

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[10] R. 44: Transcript of Hearing, at 10-14.

[11] Id.

of no more that $1,000 per month, unless the district court or EBSCO authorized such an expenditure. The injunction applies to all of Lilly's property, included any property acquired after its issuance. The district court also ordered EBSCO to post a token bond of $5,000, ostensibly to cover any damages to Lilly occasioned by the injunction. From that order, Lilly appealed to the United States Court of Appeals for the Sixth Circuit, which affirmed the district court's order.

REASONS FOR GRANTING THE WRIT

The Court should grant this petition for writ of certiorari for three reasons, each of which is addressed in the dissenting opinion to the decision of the Sixth Circuit, Appendix A.

a. The Decision of the Sixth Circuit Conflicts With The Decisions of This Court On This Important Issue Of Federal Law.

The preliminary injunction at issue violates the principles set forth by this Court in DeBeers Consol. Mines v. United States, 325 U.S. 212 (1945); Phoenix Mutal Life Ins. Co. v. Bailey, 80 U.S. (13 Wall) 616 (1871); and Adler v. Fenton, 65 U.S. 407 (1861). Federal equity jurisprudence does not permit the sequestration or impoundment of a defendant's assets merely for the purpose of securing funds for a potential money judgment. A clear explanation of why the preliminary injunction in issue is such a drastic departure from the standards pronounced by this Court is set forth in the dissenting opinion (by Ryan, J.) to the decision by the Sixth Circuit below. See Appendix A.

b. The Decision of the Sixth Circuit Creates A Conflict With Decisions By Other Federal Courts Of Appeal.

On the issue of the scope of a federal court's equitable power to freeze a defendant's assets in order to preserve a pool of funds to satisfy a potential money judgment, the decision below has created a conflict among the federal courts of appeal. The decisions in Wahlgren v. Bausch & Lomb Optical Co., 77 F.2d 121 (7th Cir. 1935); Friedling v. Freedman, 44 App. D.C. 191, 193 (1915); and Martin v. James B. Berry Sons Co., Inc., 83 F.2d 857 (1st Cir. 1936), hold that a federal district court does not have such power. If the principle announced by the Sixth Circuit is permitted to stand, it would have broad implications on all litigants who wish to freeze an adversary's assets

and limit the adversary's ability to function or even pay for his defense during the pendency of the litigation. The issue of whether a litigant may be ordered to refrain from spending his property, regardless of the purpose, is an important issue of procedural law and policy which should be addressed by the Court.

c. The Power of a Federal Court to Disregard a State Statutory Remedy Available Under Fed.R.Civ.P. 64 And Issue a Preliminary Injunction Under Fed.R.Civ.P. 65 Should Be Addressed By The Court.

The Sixth Circuit's decision raises important issues of law and comity in the context of application of the Federal Rules of Civil Procedure. This Court should address the question of whether a federal court may disregard state

statutory prejudgment remedies which are available through Fed. R. Civ. P. 64 in order to provide an equitable remedy under Fed. R. Civ. P. 65 without the requirements that the state legislature deemed necessary to protect litigants where prejudgment attachment is sought. Important issues of comity and federalism are implicated here. Again, Section I of the dissenting opinion (by Ryan, J.) to the decision of the Sixth Circuit, below, explains why an available remedy, provided by state statute, may not be ignored merely because a litigant does not like its requirements.

CONCLUSION

The judgment and decision of the Court of Appeals for the Sixth Circuit

raise important issues concerning a federal district court's equitable powers, the application of the Federal Rules of Civil Procedure, and issues of comity which should be addressed by this Court. For the reasons stated above and for the reasons set forth in the dissenting opinion to the decision of the Sixth Circuit below, Petitioner Thomas E. Lilly respectfully requests that this petition for writ of certiorari be granted.

Respectfully submitted,

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APPENDIX A

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF OHIO
WESTERN DIVISION

EBSCO INDUSTRIES, INC., Plaintiff,

vs.

THOMAS E. LILLY, Defendant and Third-Party Plaintiff,

vs.

J. RICHARD EGAN, ET AL., Third-Party Defendants.

Case No. C-1-86-340

ORDER GRANTING MOTION FOR PRELIMINARY INJUNCTION

This matter came on for consideration on the plaintiff's motion for preliminary injunction (doc. 10), which defendant has opposed (doc. 21). An evidentiary hearing was held on May 22, 1986. The Court

ruled from the Bench that a preliminary injunction should issue, at which time we stated our reasons therefor in compliance with Fed.R.Civ.P. 52(a). While we intend to supplement our oral ruling with a brief written opinion, for the record we wish to set forth the scope of the injunctive relief granted:

It is hereby Ordered that defendant Thomas E. Lilly, his agents, employees, successors, heirs, and assigns are enjoined until further Order of this Court from transferring or encumbering any of his assets other than for basic living expenses, not to exceed $1,000 per month, without the approval of the Court or of plaintiff's counsel. This Order specifically covers any securities that defendant

owns that are held by and/or has any accounts with:

Shearson American Express
Hutton
Gradison
Kidder Peabody

as well as stock and/or any interests defendant holds in the following corporations:

Sibthorp
Indiana Southern Corp.
Design Masters
Marketing Associates
Marketing Horizons
FSGC Corp.
Sarlo
Holly Corp.
Charming Shoppes, Inc.
AT & T
Electromedics
Empire-Orr
Int. Thoroughbred Breeders
E. I. DuPont
ITT
Midwest Skyline
Cedar South
Wine Merchant
Campus Care, Inc.

Plaintiff shall post a $5,000 bond as security for the payment of such costs and damages as may be incurred or suffered by any party which is found to have been wrongfully restrained by this Order.

SO ORDERED.

Filed May 22, 1986

/s/ S. Arthur Spiegel
United States District
Judge

APPENDIX B

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF OHIO
WESTERN DIVISION

EBSCO INDUSTRIES, INC., Plaintiff,

vs.

THOMAS E. LILLY, Defendant and

Third-Party Plaintiff,

vs.

J. RICHARD EGAN, et al., Third-Party

Defendants.

Case No. C-1-86-340

FINDINGS OF FACT AND CONCLUSIONS OF LAW SUPPORTING ISSUANCE OF PRELIMINARY INJUNCTION

SPIEGEL, J.:

This matter came on for consideration on plaintiff's motion for

preliminary injunction (doc. 10), which defendant opposed (doc. 21). An evidentiary hearing was held on May 22, 1986. The Court ruled from the Bench that a preliminary injunction should issue, at which time we stated our reasons therefor in compliance with Fed.R.Civ.P. 52(a). We subsequently reduced to writing the scope of the injunctive relief we granted (doc. 24). Now, mindful of our obligations under Rule 52(a), we hereby set forth our findings of fact and conclusions of law that support our issuance of the preliminary injunction.[1]

Our task is made somewhat easier by the fact that, for purposes of the May 22

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[1] We do so notwithstanding the Notice of Appeal filed June 20, 1986 (doc. 35) by defendant and third-party plaintiff Thomas E. Lilly, as we anticipate that the Sixth Circuit will remand this cause for the purpose of our entering our proposed findings of fact and conclusions of law.

hearing, defense counsel conceded that plaintiff had demonstrated a substantial likelihood of success on the merits. See infra, text discussion at p. 6. Accordingly, we will not make findings of fact and conclusions of law in that regard. Defendant also indicated a concession concerning whether the public interest would be served by the issuance of a preliminary injunction. However, because there was some equivocation on this point, we will include findings of fact and conclusions of law that relate thereto. In accordance, then, with Fed. R.Civ.P. 52(a), having considered all of the evidence, arguments, and memoranda of counsel, as well as the demeanor of witnesses, we now proceed to set forth our findings of fact and conclusions of law.

FINDINGS OF FACT

1. The plaintiff in this matter is EBSCO Industries, Inc., a Delaware corporation headquartered in Birmingham, Alabama (testimony of Thomas Stephens, president, EBSCO). In December 1983, EBSCO purchased all of the tangible and intangible personal property owned by Four Seasons Garment Corporation (Four Seasons), an Ohio corporation, whose chief executive officer and majority stockholder is defendant herein, Thomas E. Lilly. Pre-acquisition accounts and notes receivable were not part of the purchase. (Bill of Sale, Plaintiff's Exhibit 7; Asset Purchase Agreement, Plaintiff's Exhibit 1). Third-party defendant Richard D. Egan and J. Richard Egan were associates of Lilly at Four Seasons.

2. In connection with the acquisition of the assets of Four Seasons, the parties also entered into a Non-Competition and Consulting Agreement, whereby Lilly, as well at third-party defendants Richard D. Egan and J. Richard Egan, agreed not to compete with EBSCO or disclose trade secrets while being employed as consultants by EBSCO (Plaintiff's Exhibit 2).

3. Four Seasons owed a $4.5 million obligation to First National Bank of Boston Financial Company (FNB) for which Four Seasons had pledged its accounts receivable as security. Before closing the sale with EBSCO, Lilly informed EBSCO that FNB required that the obligation be paid before the operating assets of Four Seasons could be sold to EBSCO (testimony of Thomas Stephens).

4. It was represented to EBSCO that the accounts receivable being used as security for the debt had a value of $5.5 million (testimony of Stephens) and not less than $4.9 million (Certificate, Plaintiff's Exhibit 13). On December 6, 1983, Lilly and EBSCO negotiated an agreement whereby EBSCO agreed to lend $3 million to Four Seasons to be used to satisfy the debt owed to FNB (Loan and Security Agreement, Plaintiff's Exhibit 16) in return for a promissory note to Four Seasons (Plaintiff's Exhibit 12), personally guaranteed by Lilly (Plaintiff's Exhibit 11). The note was to be retired through funds received to satisfy the pre-acquisition accounts receivable.

5. It was discovered during a special examination of the records of Four Seasons in April 1986 that the accounts

receivable as of December 6, 1983 actually had had a balance of $945,000 (testimony of Lee Patrick Arceneaux, accountant, Arthur Young & Co., Birmingham, Alabama). It also was learned that while the accounts receivable from December 1983 to April-May 1986 were reported by Lilly to EBSCO to be $11,892,392.88, in fact the accounts receivable were $1,795,665.95, a discrepancy of $10,096,726.93 (testimony of Arceneaux; Plaintiff's Exhibit 29).

6. Rather than retire the $3 million promissory note with funds received to satisfy pre-acquisition accounts receivable, Lilly used $2.7 million of the post-acquisition accounts receivable generated by EBSCO after purchase of Four Seasons, and used only $475,000 of previous accounts receivable generated under

ownership of Four Seasons, to pay back the loan to EBSCO (testimony of Stephens; testimony of Arceneaux).

7. Lilly had approximately 35 to 40 computer programs specially designed for the purpose of developing and maintaining fictitious accounts receivable records (testimony of Arceneaux). Moreover, Lilly produced false documents and generated fictitious inventory tags (testimony of Stephens).

8. Companies with which Lilly is affiliated owe money to EBSCO: American Business Builders owes approximately $56,000; Design Masters owes approximately $60,000; Idis owes approximately $56,000; Image Plus owes approximately $20,000.

9. In April 1986, Lilly transferred $27,000 to the Wine Merchant Liquor Store in Memphis, Tennessee and $60,000 to Design Masters, Inc., out of business and personal investment accounts. Plaintiff contends, and documents with account balances and transfer records, that monies in addition to these likewise were transferred out to individuals, such as Lewis Harris, the proprietor of the Wine Merchant, and in the form of cash. (Plaintiff's Exhibit 30; testimony of Joseph Edward Porter II, employee at Four Seasons) (see also Plaintiff's Exhibits 33-37). At one point in their relationship, Lilly confided in his business associate that he had funds in safety deposit boxes throughout the country. Further, immediately prior to a visit from an EBSCO official, Lilly stated that

he knew of a "safe place" to which to transfer funds--that is, to Barbara Harris, wife of Lewis Harris, the proprietor of the Wine Merchant (Testimony of Joseph Edward Porter II).

10. Richard Egan notified James Stephens, president of EBSCO, of the falsifications that had taken place within Four Seasons on Easter Sunday, March 30, 1986. Defendant Lilly had cleared out his office by the evening of the next day.

CONCLUSIONS OF LAW

In considering whether to grant a preliminary injunction, this Court must review four factors that are well-established by Sixth Circuit case law. Those factors examine

(1) Whether the plaintiff has shown a strong or substantial likelihood or probability of success on the merits;

(2) Whether the plaintiff has shown irreparable injuries;

(3) Whether the issuance of a preliminary injunction would cause substantial harm to others;

(4) Whether the public interest would be served by issuing a preliminary injunction.

Warner v. Central Trust Co., 715 F.2d 1121, 1123 (6th Cir. 1983). See Friendship Materials, Inc. v. Michigan Brick, Inc., 679 F.2d 100, 102 (6th Cir. 1982); Mason County Medical Association v. Knebel, 563 F.2d 256, 261 (6th Cir. 1977). As mentioned, for purposes of the preliminary injunction hearing only, defendant Lilly conceded that plaintiff demonstrated a substantial likelihood of success on the merits. Accordingly, we

make conclusions of law corresponding to the findings of fact regarding the remaining three factors.

A. Irreparable Harm

There is overwhelming evidence based on the testimony of witnesses, and the exhibits admitted into evidence, that defendant Lilly defrauded plaintiff while operating the Four Seasons Garment Company. Lilly, orally and through false financial statements, grossly overstated the Four Seasons accounts receivable. Relying upon Lilly's representations, EBSCO lent Lilly's company $3 million in return for a promissory note personally guaranteed by Lilly. Through a complex and premeditated scheme, Lilly paid EBSCO back with $2.7 million in accounts receivable generated by EBSCO after

acquiring Four Seasons. To carry out the scheme, Lilly personally falsified the amount of income alleged to be from the old accounts receivable and perpetrated the deception by manipulating the company data processing system to accept and print a false accounts receivable list, and by printing other false documents and generating fictitious inventory tags. Moreover, Lilly diverted Four Seasons funds and property into some of his own businesses and misapplied company funds to his own personal uses. Clear and convincing evidence shows that Lilly attempted to move assets from out of the reach of his creditors. Plaintiff documented several transfers of money to Lewis Harris of Memphis, Tennessee, the alleged "safe place" of which Four Seasons employee Porter spoke in his

testimony at the hearing. If, during this litigation, Lilly were to continue this activity by manipulating or moving any assets, plaintiff would face irreparable harm.

Defendant contends that the United States Supreme Court established long ago in DeBeers Consolidated Mines Ltd. v. United States, 325 U.S. 212 (1945), that a preliminary injunction could not be issued to restrain a defendant from withdrawing, selling, transferring, or disposing of any property belonging to them for the purpose of protecting any future judgment that might be won. We disagree with defendant that DeBeers is applicable to the instant case. In DeBeers, the United States sought a preliminary injunction against certain foreign corporations because of the

injury it would suffer if same withdrew their assets from this country, thereby removing property that the United States could attach to enforce any Court order or decree it eventually might secure. Id. at 215. The difficulty with the injunction, according to the Court, was that "[i]t is not an injunction in the cause, and it deals with a matter lying wholly outside the issues in the suit. It deals with property which in no circumstances can be dealt with in any final injunction that may be entered." Id at 220. In United States v. First National City Bank, the Court upheld issuance of an injunction enjoining respondent "from transferring any property or rights to property of [the foreign corporation] now held by it or by any branch offices within or without the United States . . . ."

379 U.S. 378, 380 (1965). The Court distinguished DeBeers by noting that First National involved property that would be "the subject of the provisions of any final decree in the cause." Id. at 395. The Court in First National also viewed the temporary injunction as a reasonable measure to preserve the status quo. Id. Even in DeBeers the Court explicitly had stated that "[a] preliminary injunction is always appropriate to grant intermediate relief on the same character as that which may be granted finally." 325 U.S. at 220. We think this case falls under the exception to DeBeers as discussed in First National because this case, like First National, involves property that could be the subject matter of a final injunction.

While First National involved an Internal Revenue assessment and is therefore not fully controlling, the general principles regarding preservation of the status quo and the avoidance of dissipation of assets are clearly authoritative in this case. USACO Coal Co. v. Carbomin Energy, Inc., 539 F.Supp. 870, 816 (W.D. Ky.), aff'd, 689 F.2d 94 (6th Cir. 1982). Plaintiff's right to damages and an accounting would be compromised and thus it would be harmed if defendant were successful in removing his assets. Like the Sixth Circuit in USACO, we do not believe that Ohio's attachment statute (Ohio Rev. Code §§2715.01 et seq.) can "provide plaintiff[ ] with adequate protection against the probability of continued disreputable conduct that would result in the dissipation and concealment of

assets . . . ." 689 F.2d at 99. Therefore, plaintiff does not have an adequate remedy under Ohio law.

B. Harm to Defendant and the Public Interest

The Court was not presented with any evidence at the May hearing that indicates that the defendant Lilly would be harmed by issuance of the preliminary injunction. In defendant's Memorandum in Opposition to Plaintiff's Motion for Preliminary Injunction, defendant contends that "the injunction sought here would cripple Lilly's businesses by preventing him from allocating his resources to keep them afloat" (doc. 21 at 9).

2/ During the evidentiary hearing, the Court questioned plaintiff why Ohio Rev. Code §§ 2715.01 et seq. could not be employed to resolve this dispute rather than resorting to equitable relief. The plaintiff responded on two fronts:

Defendant did not support this contention at the hearing and it is our view that defendant is not vulnerable to such a result. Because the nature of this case involves fraud and embezzlement, as has been conceded for the purposes of this lawsuit, the freezing of defendant Lilly's assets is in effect the freezing of plaintiff's assets. The result is a situation akin to a constructive trust

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Footnote 2 continued

primarily, that whenever defendant is questioned about his business activities, he invokes his Fifth Amendment right to remain silent with the result that plaintiff does not know what assets to attach under the statute; secondly, that the attachment statute requires that a bond be posted in double the amount of recovery being sought. See Ohio Rev. Code §2715.044. Given that plaintiff seeks redress for an alleged embezzlement of some $2.7 million as well as for a soured purchase transaction in which the value of his business was overstated by over $10 million, we concluded that it would indeed be onerous to require the plaintiff to pursue such a route.

such that no substantial harm will visit defendant or his business enterprises. Additionally, plaintiff has been ordered to post a bond as security for payment of costs and damages incurred by any party that is found to have been wrongfully restrained by the preliminary injunction. Moreover, the injunction does not unnecessarily restrain the ordinary personal expenses of defendant Lilly; specifically, it allows him to transfer or encumber $1,000 of his assets for basic living expenses every month without approval of the Court or of plaintiff's counsel.

Finally, we find that the public interest would be served by the issuance of a preliminary injunction. The evidence overwhelmingly disclosed fraudulent conduct on the part of defendant. Moreover,

the abrupt nature of Lilly's departure from Four Seasons enhances the suspicious nature of his ordering of his affairs. Such conduct should not be rewarded, but instead should be restrained in recognition of the public policy against fraudulent activity and in an effort to protect the public from its fallout.

Accordingly, for the above-stated reasons, defendant Thomas E. Lilly is restrained as indicated in our Order granting motion for preliminary injunction dated May 22, 1986 (doc. 24).

SO ORDERED.

/s/ S. Arthur Spiegel
United States District
Judge

Filed August 1, 1986

RECOMMENDED FOR FULL TEXT PUBLICATION
See. Sixth Circuit Rule 24

No. 86-3595

UNITED STATES COURT OF APPEALS

FOR THE SIXTH CIRCUIT

EBSCO INDUSTRIES, INC.,
Plaintiff-Appellee,

v.

THOMAS E. LILLY,
Third-Party-Plaintiff. Defendant-Appellant,
J. RICHARD EGAN; RICHARD D. EGAN; AND J. EDWARD PORTER, III,
Defendants.

ON APPEAL from the United States District Court for the Southern District of Ohio.

Decided and Filed February 23, 1988

Before: MERRITT and RYAN, Circuit Judges; and BROWN, Senior Circuit Judge.

MERRITT, Circuit Judge, delivered the opinion of the court, in which BROWN, Senior Circuit Judge, joined. RYAN, Circuit Judge, (pp. 8-14) delivered a separate dissenting opinion.

MERRITT, Circuit Judge. This appeal raises questions under Rule 64, Fed. R. Civ. P. which provides for prejudg-

ment attachment to preserve assets for the payment of anticipated judgments and under Rule 65, which provides for injunctive relief. Specifically the issue is whether the District Court may use its injunctive powers under Rule 65 instead of its attachment authority under Rule 64 in order to preserve assets prior to trial or judgment, and if so, under what circumstances?

Rule 64 provides that "during the course of an action, all remedies . . . for . . . seizure of . . . property for the purpose of securing satisfaction of the judgment ultimately to be entered . . . are available . . . in the manner provided by the law of the state in which the district court is held . . . ." In the instant case, the plaintiff made a strong evidentiary showing that the defendant, Lilly, had defrauded the plaintiff company of approximately $3 million in connection with the sale of Lilly's textile manufacturing company to plaintiff. Lilly, asserting his privilege under the Fifth Amendment, refused to answer questions concerning his assets and their disposition. District Judge Arthur Spiegel found a strong likelihood that Lilly was attempting to conceal and dispose of assets in order to defeat execution of the final judgment in plaintiff's favor, which the Court expected to be entered after trial.

Instead of entering an order setting in motion attachment procedures under Ohio law, as provided in Rule 64, the District Court entered an injunction under Rule 65 as follows:

> It is hereby Ordered that defendant Thomas E. Lilly, his agents, employees, successors, heirs, and assigns are enjoined until further Order of this Court from transferring or encumbering any of his assets other than for basic living expenses, not to exceed $1,000 per month, without the approval of the Court or of plaintiff's counsel.

The District Court made clear, explicit and complete specific findings of fact and conclusions regarding irreparable injury, likelihood of success on the merits and the other fac-

tors required for the issuance of a preliminary injunction under *Warner v. Central Trust Co.*, 715 F.2d 1121, 1123 (6th Cir. 1983). Judge Spiegel's finding, located in a footnote of his opinion, concerning the inadequacy of the legal attachment remedies provided under Ohio law and Rule 64 was as follows:

> Whenever defendant is questioned about his business activities, he invokes his Fifth Amendment right to remain silent with the result that plaintiff does not know what assets to attach under the statute; secondly, that the attachment statute requires that a bond be posted in double the amount of recovery sought. . . . Given that plaintiff seeks redress for . . . $2.7 million as well as for a soured purchase transaction . . . it would indeed be onerous to require the plaintiff to pursue such a route.

The question on appeal is whether this finding was sufficient for the exercise of the Court's equity powers.

Ohio's attachment provisions, § 2715.01-.56, permit a court to issue an attachment of defendant's property if the defendant is about to remove his property from the jurisdiction of the court, with the intent to defraud his creditors; or if he is about to convert his property into money to place it beyond the reach of creditors; or if he has property which he is concealing; or if he has disposed of his property with the intent to defraud creditors. Ohio Rev. Code Ann. § 2715.01(6)-(9) (Baldwin 1984). Once the court authorizes prejudgment attachment, plaintiff must pay a bond equal to the value of the property to be attached, or, if not known, twice the value of plaintiff's claim. § 2715.044, .26 The court's order of attachment is then delivered to the levying officer who, without delay, will go to the location of the property, make an inventory and appraisal of its value, and take it into custody if personal property, or conspicuously place notice of attachment on it if real property. § 2715.05-.09.

Ohio state courts have held that the attachment provisions provide a legal, as distinguished from an equitable, prejudgment remedy. *Haines v. Public Finance Corp.*, 70 Ohio App. 2d 89, 218 N.E.2d 727, 729 (1966); *Cheney v. The Maumee Cycle Co.*, 64 Ohio St. 205, 214, 60 N.E. 207 (1901). *See also* 7 J. Moore & J. Lucas, *Moore's Federal Practice* § 64.04[3], at 64-19-20 (1987); C. Wright & A. Miller, *Federal Practice and Procedure* § 2932 (1973). Before exercising their equitable injunctive powers courts in Ohio have traditionally held that the moving party must show that he has no adequate legal remedy. *Adams v. Long*, 60 N.E.2d 629, 632, 42 O.L.A. 449, 451 (Ohio Ct. App. 1944); *see also Int'l Union, et al. v. Lester Engineering Co.*, 575 F. Supp. 797, 801 (N.D. Ohio 1982). Where Ohio statutes afford the party a legal remedy, a determination must be made that these statutory remedies are inadequate before a court can implement its equity powers and issue an injunction. *Blythin v. Zangerle*, 83 Ohio App. 355, 77 N.E.2d 379, 384 (1947); *Adams v. Long*, 60 N.E.2d at 632.

In addition, Ohio courts have specifically held that the legal remedy of attachment must be shown inadequate before an equitable remedy may issue. *Jebb Realty Service Co. v. McIntosh*, 26 Ohio App. 92, 93-94, 159 N.E. 143 (1926); *Card Fabrique Co. v. Stanage*, 50 Ohio St. 417, 34 N.E. 410 (1893); *Secor v. Witter*, 39 Ohio St. 218, 235 (1883); *Endel v. Leibrock*, 33 Ohio St. 254, 269 (1877). In *Jebb Realty*, the court ruled that the lower court should not have exercised its equity power to appoint a receiver "to accomplish what should have been accomplished by a writ of attachment." 26 Ohio App. at 94.

The Michigan Supreme Court has also ruled on this issue in the same way:

> The law processes of . . . attachment would have obviated the necessity of the injunction. . . . Plaintiff herein had a full, complete and adequate remedy

> at law and there was no showing that there was some feature of the case that would bring it peculiarly within the province of a court of equity.

Christian v. Porter, 340 Mich. 300, 65 N.W.2d 779, 782 (1954).

Although federal courts have rarely examined when, in a given case, Rule 64 attachment should issue instead of Rule 65 injunction, in *Dorfmann v. Boozer*, 414 F.2d 1168, 1171-72, 1174 (D.C. Cir. 1969), the court expressly held that where the legal remedy of attachment is adequate, an injunction should not be granted. In *Dorfmann*, the court reversed the lower court's grant of a preliminary injunction because the moving party had not shown that the attachment remedy was not adequate. The court stated:

> [A]ppellees now attempt to seize upon this action of appellants not only to get around the attachment statute, but actually to obtain relief which they could not get under that statute.

Id. at 1172. The court explained:

> The great equitable power to enjoin a party *pendente lite* should not be exercised unless it is manifest that the normal legal avenues are inadequate, that there is a compelling need to give the plaintiff the relief he seeks, and that the injunction will not wreak greater harm on the party enjoined.

Id. at 1174; *see also Mitchell v. Lay*, 48 F.2d 79, 83 (9th Cir. 1931); *Taunton Municipal Lighting Plant v. Dept. of Energy*, 472 F. Supp. 1231, 1233 (D. Mass. 1979); *Berman v. Narragansett Racing Ass'n*, 48 F.R.D. 333, 336 (D.R.I. 1969).

No Sixth Circuit case has explicitly held that before a court issues a preliminary injunction it must find in addition to the other criteria for an injunction, that the legal remedy of attachment is inadequate to redress the moving party's con-

cerns. However, the Sixth Circuit has held generally that an injunction may not issue if there is an adequate remedy at law. *Gilley v. United States*, 649 F.2d 449, 454 (6th Cir. 1981); *Detroit Newspaper Publishers Ass'n v. Detroit Typographical Union No. 18*, 471 F.2d 872, 876 (6th Cir. 1971); *Travis v. Pennyrile Rural Electric Corp.*, 399 F.2d 726, 729 (6th Cir. 1968); *see also Beacon Theatres v. Westover*, 359 U.S. 500, 506-07 (1958). In addition, the Sixth Circuit recently held in *USACO Coal Co. v. Carbomin Energy*, 689 F.2d 94, 99 (6th Cir. 1982), that a state's attachment statute could not provide adequate protection to plaintiff and therefore upheld the district court's injunction.

Our view that a preliminary injunction may not be granted unless there are valid findings that the legal remedy provided by the state's attachment statutes under Rule 64 is inadequate, is based on long-standing theories of equity jurisdiction. In his treatise *Equity Jurisprudence*, Pomeroy advises us:

> [I]t is solely because these legal remedies are, under the assumed circumstances, inadequate to do complete justice, . . . that the courts of equity also have the power to interfere and to award . . . remedies . . . .

J. Pomeroy, I *Equity Jurisprudence* 216-17 (1881).

Although the District Court in this case made substantial and complete findings and conclusions on other factors supporting the issuance of a preliminary injunction, it would have been well for it to make more complete findings on the inadequacy of the attachment remedy. The Court found that the defendant had taken specific steps to conceal assets and had refused to disclose what assets he has or where they are located, making attachment difficult if not impossible. It also found that making a surety bond for twice the amount of the claim would be extremely costly and unnecessary under the circumstances. In addition, Ohio's attachment statutes do not

provide an adequate remedy because: (1) They do not apply to assets located outside of Ohio; thus EBSCO must initiate attachment proceedings in each state where defendant owns property. (2) If plaintiff can find that defendant owns securities which it is concealing, EBSCO must garnish or enjoin securities brokers or whoever possesses the securities so that Ohio levying officers can obtain possession of stock certificates. (3) Delay resulting from the attachment process will provide additional time for defendant to dissipate assets. (4) The bond premium in a case such as this one involving claims for some $3 million in assets taken by fraud would be enormous. These factors, along with the reasons stated by the District Court, plus its clear findings of fraud, are sufficient to satisfy the requirement that the attachment remedy be shown to be inadequate. We therefore affirm the judgment of the District Court.

RYAN, Circuit Judge, dissenting. In my judgment, the district court was without authority to issue the preliminary injunction the court approves today. The authorities in support of that view are marshalled in a clear, coherent, and persuasive fashion in my brother's opinion for the court. Unfortunately, the dispositive final paragraph for affirmance is antithetical to the discussion that proceeds it and, in my view, offers no basis in law to justify the court's conclusion.

The issue, as correctly stated in the majority opinion, is "whether the district court may employ its injunctive powers under Fed. R. Civ. P. 65 instead of its attachment authority under Rule 64 in order to preserve assets prior to trial or judgment, and, if so, under what circumstances." The answer is no, not as it was done in this case. Most of the reasons are clearly spelled out in my brother's opinion.

I.

It is uncontroverted that the district court issued its injunction in this case solely to secure a fund from which the plaintiff will be able to satisfy a money judgment if one is entered in its favor following trial. Stated otherwise, the purpose of the injunction is to assure that, come judgment day, the defendant will be collectible.

As my brother correctly observes (it is difficult to avoid reference to the majority opinion since, save for the final paragraph, it states much of the case for this dissent concisely, eloquently, and correctly), Rule 64 provides that state law determines the remedies available in a federal court for the seizure of property to secure a fund from which to satisfy an anticipated money judgment. In this case, that law is Ohio Rev. Code Ann. § 2715.01-.56 which provides for prejudgment attachment. In addition, it is settled in Ohio, as my brother points out, that the attachment remedy may not be bypassed and resort had to equitable relief merely to secure a fund for the purpose of satisfying an anticipated judgment,

unless the moving party demonstrates that the attachment statute is not an adequate remedy. *See Blythin v. Zangerle*, 83 Ohio App. 355, 77 N.E.2d 379, 384 (1947); *Adams v. Long*, 60 N.E.2d 629, 632, 42 O.L.A. 334 (Ohio App. 1944); *Jebb Realty Service Co. v. McIntosh*, 26 Ohio App. 92, 93-94, 159 N.E. 143 (1926).

Here, EBSCO has an adequate legal remedy under Ohio's attachment statute. But the district court determined that the attachment remedy was "inadequate" for two reasons: (1) the plaintiff, when asked by defendants' attorneys about his personal assets, invoked the fifth amendment privilege against self-incrimination; and (2) the attachment statute requires that the party seeking attachment post a bond in an amount equal to the value of the asset to be attached or double the amount of the judgment sought, and that such a bond, in this case, is "onerous." For those reasons, the district court declared the attachment statute to be an inadequate remedy at law and proceeded to enter the sweeping injunction under review.

The Ohio legislature, in enacting the attachment statute, fixed the formula for determining the amount of bonds to be posted under the statute. It is not for the district court or this court to effectively overrule or disregard that determination by concluding that when the amount of the bond is very substantial because the amount of the judgment sought is substantial, the attachment statute is therefore an inadequate legal remedy. The defendant, the district court, and this court, have cited no authority to support the novel notion that Ohio plaintiffs have no adequate legal remedy in attachment for cases in which the amount the plaintiffs seek is in the millions, thus requiring a security bond in the multimillions.

Moreover, the district court's findings of fact are wholly inadequate to support its conclusion that the plaintiff does not have an adequate remedy under the Ohio attachment

statute. Although the court observed that, in its judgment, the Ohio attachment statute would not provide the plaintiff "with adequate protection against the probability of continued disreputable conduct that would result in the dissipation and concealment of assets . . .," it did not explain why it reached that conclusion. The defendant's refusal to tell the plaintiff where the defendant's assets are located, and the fact that the plaintiff seeks a judgment in an amount which, if it wishes to seize defendant's assets even before it proves its entitlement to judgment, requires, under the statute, a very substantial bond, do not, alone or in combination, demonstrate the inadequacy of Ohio's attachment statute; they demonstrate at best that the plaintiff has failed thus far to locate any attachable assets, and that the legislative judgment as to the amount of the required prejudgment attachment bond is more than the plaintiff would like to post.

II.

But even if the court were correct in its conclusion that the Ohio attachment statute is an inadequate legal remedy in order to secure a fund of property for post-judgment levy, the injunction issued by the court is entirely beyond the court's lawful power.

A federal court may not issue a temporary injunction restraining a defendant in a suit for money damages from disposing of substantially all of his, her, or its assets, identifed and unidentified, in hand and after acquired, solely to assure the existence of a fund from which the plaintiff, if successful, may later satisfy favorable money judgment. *DeBeers Consol. Mines v. United States*, 325 U.S. 212 (1945); *Wahlgren v. Bausch & Lomb Optical Co.*, 77 F.2d 121 (7th Cir. 1935); *Martin v. James B. Berry Sons Co., Inc.*, 83 F.2d 857 (1st Cir. 1936).

The *DeBeers* Court explained why:

> Every suitor who resorts to chancery for any sort of relief by injunction may, on a mere statement of

> belief that the defendant can easily make away with or transport his money or goods, impose an injunction on him to use so much of his funds or property as the court deems necessary for security or compliance with its possible decree. And, if so, it is difficult to see why a plaintiff in any action for a personal judgment in tort or contract may not, also, apply to the chancellor for a so-called injunction sequestering his opponent's assets pending recovery and satisfactory of a judgment in such law action. No relief of this character has been thought justified in the long history of equity jurisprudence.

325 U.S. at 222-23.

What a federal court *may* do, in an appropriate case to assure that misappropriated funds will not be dissipated pending trial and judgment, is impose a constructive trust upon the misappropriated property in the hands of the wrongdoer or upon property into which the misappropriated funds can be directly traced. *United States v. Brimberry*, 779 F.2d 1339 (8th Cir. 1985). That is especially true when it is alleged, as it is here, that the defendant wrongdoer has acquired funds belonging to the plaintiff, in violation of a fiduciary duty owed the plaintiff. *See McCandless v. Furland*, 296 U.S. 140 (1935); *USACO Coal Co. v. Carbomin Energy, Inc.*, 689 F.2d 94 (6th Cir. 1982). It is well-settled, however, that such a constructive trust, must be imposed upon the specific ascertainable assets—the *res*—missappropriated from the plaintiff and now in the defendant's hands or upon property into which the misappropriated funds have been converted. *See* Dobbs, *Remedies*, § 4.3, pp. 240-43 (West 1980):

> This device [constructive trust] is used only when property in some form can be identified as belonging in good conscience to the plaintiff.[12] If defendant obtains Blackacre from the plaintiff by fraud, sells it and dissipates the money, this gives the plaintiff

> no claim to other property owned by the defendant, and it may not be said that the defendant is a constructive trustee of such other property.[13] In such a case, he is liable for damages .... [T]he constructive trust can be imposed only when there is some specific property identified as belonging, in equity and conscience, to the plaintiff.
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> ---
>
> [12]Occasionally courts speak of a constructive trust even though there is no *res* or property to which a trust might attach. This makes sense only on the assumption that the court is referring to the substantive principle against unjust enrichment, as grounds for granting an ordinary judgment.

(Footnote 13 omitted.)

But that is not this case at all. Plaintiff has made no attempt whatever to trace the funds said to have been misappropriated from it into a specific *res* which might be the object of a constructive trust. Indeed, the testimony introduced at the hearing before the district court on the plaintiff's petition for an injunction is that there is no evidence that the defendant actually received any of the misappropriated funds for which the plaintiff seeks recovery, but instead fraudulently diverted them to the First National Bank in payment of the three million dollar promissory note made by Four Seasons and guaranteed by the defendant.

The learned district judge appears to have acknowledged, albeit somewhat obliquely, that the court's power to issue an injunction solely to secure a corpus from which the plaintiff might later satisfy a money judgment is limited to an injunction which imposes a constructive trust upon a specific *res*. The court stated in its Findings of Fact and Conclusions of Law:

> Because the nature of this case involves fraud and embezzlement, as has been conceded for the purposes of this lawsuit, the freezing of defendant Lilly's assets is in effect the freezing of plaintiff's assets. The result is a situation *akin* to a constructive trust such that no substantial harm will visit defendant or his business enterprises. (Emphasis added.)

The difficulty with that observation, of course, is that there is no evidence in the record that the "freezing of defendant Lilly's assets is in effect the freezing of plaintiff's assets" because, as has been observed, the bulk of the evidence is that the misappropriated funds are not in Lilly's hands, and never were, but have been diverted to First National Bank in payment of the aforementioned promissory note. In all events, "freezing the defendant Lilly's assets" by enjoining him from transferring or encumbering any of his assets presently in hand, and from spending any after acquired income, in excess of $1,000 a month for living expenses, is not the imposition of a constructive trust upon a specific identifiable *res* once in the hands of the plaintiff and now traceable to the defendant, and it is not "akin" to it. Indeed, the sweeping injunction in this case was entered specifically because, as the district court put it, "the plaintiff does not know what assets to attach. . . ." Both the district court and this court rely upon *USACO Coal Co.*, 689 F.2d 94, to justify the injunction that has been issued. A careful reading of *USACO Coal Co.* reveals why it is no authority for what has been done here. In that case, one Schierack was alleged to have breached his fiduciary duty as a promoter of a newly organized plaintiff corporation by diverting funds raised for the corporate promotion to himself and to several other corporations controlled by him. The plaintiffs brought a civil RICO action against the individual promoter and the several corporations controlled by him into which the plaintiffs' funds had been diverted. This court approved the issuance of an injunction, freezing in place the assets, *not* of the individual wrongdoers,

but of the specifically identified defendant corporations into which the promoter had diverted the plaintiffs' fund. This court troubled to observe that it was not approving an injunction issued for the purpose of creating a collectible defendant, as in this case, but was approving the imposition of a constructive trust upon specific, identifiable assets in the possession of identified corporate defendants:

> It is entirely clear that the district court issued the injunction freezing defendants' assets in order to protect the rights of the plaintiff corporations and their shareholders to restitution of funds obtained by [the individual promoter] in breach of his promoter's fiduciary duty. The injunction was not issued in order to secure a RICO treble damages award that might ultimately result from count one of the complaint, but rather was issued to protect rights to reach the defendants' property as a result of the allegation of breach of fiduciary duty contained in count two of the complaint.... The injunction here preserves assets for which the defendants may be accountable under a constructive trust.

USACO Coal Co., 689 F.2d at 97. Here, indisputably, the injunction was issued solely for the purpose of "secur[ing] a ... damages award."

If EBSCO wished to attach or sequester defendant's assets, it was obligated, under Rule 64, to comply with the Ohio statutory requirements for posting a bond. If it wished instead, to impose a constructive trust, it was obligated to identify and "freeze" an ascertainable *res* that is traceable back to the plaintiff. The district court required neither in this case, with the result that the injunction issued is beyond its lawful authority.

I would reverse and remand for specific findings concerning the *res* of the constructive trust or, in the alternative, for an

order that plaintiff deposit a bond or cash deposit meeting the requirements of Ohio Rev. Code Ann. § 2715.01.

OHIO REVISED CODE

2715.01 Grounds of attachment

(A) An attachment against the property, other than personal earnings, of a defendant may be had in a civil action for the recovery of money, at or after its commencement, upon any one of the following grounds:

(1) Excepting foreign corporations which by compliance with the law therefore are exempted from attachment as such, that the defendant or one of several defendants is a foreign corporation;

(2) That the defendant is not a resident of this state;

(3) That the defendant has absconded with the intent to defraud his creditors;

(4) That the defendant has left the county of his residence to avoid the service of a summons;

(5) That the defendant so conceals himself that a summons cannot be served upon him;

(6) That the defendant is about to remove his property, in whole or part, out of the jurisdiction of the court, with the intent to defraud his creditors;

(7) That the defendant is about to convert his property, in whole or part, into money, for the purpose of placing it beyond the reach of his creditors;

(8) That the defendant has property or rights in action, which he conceals;

(9) That the defendant has assigned, removed, disposed of, or is about to dispose of, his property, in whole or part, with the intent to defraud his creditors;

(10) That the defendant has fraudulently or criminally contracted the debt, or incurred the obligations for which suit is about to be or has been brought;

(11) That the claim is for work or labor;

(12) That the defendant has not complied with the provisions of sections 1306.01 to 1306.09 of the Revised Code, relating to bulk transfers.

2715.03 Application after commencement of action for money

A plaintiff in an action for the recovery of money, upon or at any time after the commencement of the action, may apply to the court by written motion for the attachment of property, other than personal earnings, of the defendant. The motion shall have attached to it the affidavit of the plaintiff, his agent, or attorney, which shall set forth all of the following:

(A) The nature and amount of the plaintiff's claim, and if the claim is based upon a written instrument, a copy of that instrument;

(B) The facts that support at least one of the grounds for an attachment contained in section 2715.01 of the Revised Code;

(C) A description of the property sought and its approximate value, if known;

(D) To the best of plaintiff's knowledge, the location of the property;

(E) To the best of the plaintiff's knowledge, after reasonable investigation, the use to which the defendant has put the property and that the property is not exempt from attachment or execution.

(F) If the property sought is in the possession of a third person, the name of the person possessing the property.

2715.044 Plaintiff to file bond before attachment ordered; exception for nonresident defendant; indigent plaintiff

An order of attachment issued by a court shall not be effective until the plaintiff that filed the motion for attachment files with the court a bond to the defendant against whom the motion was filed, executed by the plaintiff's surety

in an amount twice the approximate value of the property to be attached under the order, to the effect that, should judgment be issued against the plaintiff, the plaintiff will return the property taken or pay the value so assessed, at the election of the defendant, and also pay the damages suffered by the defendant as a result of the taking and detention of, and any injury to, the property and the costs of the action. If the plaintiff does not know the approximate value of the property sought to be attached under the order, or if the identity of the property to be attached is not known, the bond shall be in an amount twice that of the plaintiff's claim, as indicated in the plaintiff's affidavit filed pursuant to section 2715.03 of the Revised Code.

In lieu of the bond, the plaintiff may deposit with the clerk of the court cash in the same amount.

When the ground of attachment is that the defendant is a foreign corporation, or not a resident of this state, the order of attachment may be issued without a bond.

If the plaintiff is indigent, the court may, on motion of the plaintiff or on its own motion, waive the bond required this section or may set the bond in a lower amount, as fairness requires.

Supreme Court, U.S.
FILED
JUL 20 1988
JOSEPH F. SPANIOL, JR.
CLERK

No. 87-2032

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1987

THOMAS E. LILLY,

Petitioner,

vs.

EBSCO INDUSTRIES, INC.,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

RESPONDENT EBSCO INDUSTRIES, INC.'S BRIEF IN OPPOSITION

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QUESTION PRESENTED FOR REVIEW

Whether a district court, within its discretion, may issue a preliminary injunction restricting the disposition of a defendant's assets where:

1. The unrefuted evidence demonstrates the defendant's embezzlement and breach of fiduciary duties;
2. The defendant stipulates that the plaintiff has a substantial likelihood of success on the merits of all its claims;
3. The plaintiff seeks an accounting from the defendant;
4. The evidence shows the defendant's transfer and dissipation of assets;
5. The defendant invokes his Fifth Amendment privilege upon deposition, and fails to attend the preliminary injunction hearing; and,
6. Available state pre-judgment attachment remedies do not provide plaintiff with an adequate remedy at law.

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RESPONDENT EBSCO INDUSTRIES, INC.'S BRIEF IN OPPOSITION

Respondent, EBSCO Industries, Inc., respectfully requests that this Court deny the Petition for Writ of Certiorari seeking review of the Order of the United States Court of Appeals for the Sixth Circuit in this case.

STATEMENT OF THE CASE

This is an action for fraud, material breach of representations, breach of contract, negligence, breach of fiduciary duty, and for an accounting by EBSCO Industries, Inc. (EBSCO) against Thomas E. Lilly (Lilly), arising out of the sale of the assets of Four Seasons Garment Corporation (Four Seasons) to EBSCO by Lilly, and out of Lilly's activities as Vice President of EBSCO and General Manager of Four

Seasons following that sale. Evidence presented at the May 22, 1986 hearing on EBSCO's Motion for Preliminary Injunction established the following facts.

Four Seasons was a Mason, Ohio manufacturer/wholesaler of custom sporting and leisure apparel. EBSCO is a diversified Birmingham, Alabama based company with interests in subscription reading services, printing, advertising displays, publishing and various other products and services. On December 6, 1983, EBSCO purchased certain assets and the name of Four Seasons from Lilly and his associates. (R. 44, Ex. 1). At that time, Lilly owned the majority of Four Seasons stock, and was the Chairman of its Board of Directors. Under the agreement, Lilly and his associates were to remain at Four Seasons under consulting agreements, and were to operate the company as a division of EBSCO. The sellers also entered into extensive agreements not to compete with EBSCO. (R. 44, Exs. 2-4).

The acquisition did not include purchase of Four Seasons' accounts receivable. (R. 44, Ex. 1; R. 44 at 32). On the eve of the closing, Lilly approached EBSCO with the proposal that EBSCO lend Four Seasons and Lilly Three Million Dollars to be used to satisfy their obligations to the First National Bank of Boston to which the receivables were pledged. (R. 44 at 33-34). It was represented to EBSCO that the receivables had a value of approximately Five and one half Million Dollars. (R. 44 at 33-34). Based upon this representation and upon a written certification that the accounts receivable were not less than Four Million Nine Hundred Thousand Dollars, EBSCO lent Three Million Dollars to Four Seasons Garment Corporation in return for a promissory note from that corporation, guaranteed by Lilly. (R. 44 at 34; R. 44, Exs. 5, 10-13). Under the agreement, Lilly was to retire the note by monthly installments equal to the payments received upon such accounts receivable in each month. (R. 44 at 37-38).

Unknown to EBSCO, Lilly had knowingly overstated the Four Seasons accounts receivable by approximately Four Million Dollars, by creating fictitious accounts in order to ob-

tain the financing that his loan from EBSCO was to pay off. (R. 44 at 86-89). Since there were not enough actual receivables to retire the note, Lilly contrived a scheme of embezzlement to perpetuate and conceal his original fraud. Under this scheme, he applied Two Million Seven Hundred Thousand Dollars in receipts from accounts generated *after* EBSCO's purchase to retire the Three Million Dollar note; *thus paying EBSCO with its own money*. (R. 44 at 43, 62, 84-86; R. 44 Ex. 28). To do this he submitted monthly reports to EBSCO in which he personally falsified the amount of income alleged to be from the "old" accounts. (R. 44 at 40-41, 89-90; R. 44, Ex. 29).

After all payments on the note were made, Lilly's fraud continued. Since he had used current income to satisfy an antecedent obligation, he had to persist in creating fictitious accounts receivable and inventory to avoid disclosure that the business was losing money, and that the receivables had been misapplied. (R. 44 at 40-41, 89-90; Ex. 29). This was done by Lilly in several ways.

First, by conspiring with an outside computer consultant and others, the company data processing system was manipulated to accept and print a false accounts receivable list. (R. 44 at 42, 91-92). Second, Lilly and others produced bogus invoices and other documents which confirmed the false accounts receivable print-out and misled auditors. (R. 44 at 89-92). Third, Lilly arranged for many of the outside auditors' accounts receivable confirmations to be sent to and returned by persons acting on Lilly's instruction (R. 44 at 42).

Lilly's fraud collapsed in the last few days of March, 1986. Unable to convince one of his involved associates, Richard Egan, to participate any longer, Lilly cleaned out his office and departed on March 31, 1986. Egan then went to EBSCO management and described the wrongdoing in great detail. (R. 44 at 43-44).

EBSCO's efforts to obtain discovery from Lilly were frustrated by his invocation of the Fifth Amendment privilege

against self-incrimination. (R. 22). However, EBSCO was able to determine that Lilly had liquidated his securities holdings and had transferred the proceeds therefrom to a Memphis, Tennessee liquor store owned in part by Lilly, and operated by his brother-in-law, Lewis Harris. From there much of the money was taken out by Mr. Harris. (R. 44, Exs. 30-36).

Testimony of J. Edward Porter indicated that, one week prior to his departure, Lilly stated that he had a "safe place" to transfer funds if found out by EBSCO. That "place" was described as Barbara Harris, Lewis Harris' wife. (R. 44 at 72).

The final items of evidence were records of Society Bank, the admissibility of which was stipulated. Those records disclosed Lilly's unauthorized withdrawal of funds from Midwest Skyline, Inc. and their deposit in Design Masters, another business of Lilly's. These documents were introduced as evidence of Lilly's past dissipation of funds to which he was not entitled and were probative of EBSCO's entitlement to the relief granted by the district court.

Based upon the evidence, the district court issued its Preliminary Injunction (R. 24) and subsequent Findings of Fact and Conclusions of Law (R. 41). The Court of Appeals affirmed.

REASONS FOR DENYING THE WRIT

Petitioner herein essentially adopts and urges the correctness of the dissenting opinion in the Sixth Circuit. The gist of that dissent is that a defendant's pre-judgment disposition of assets may be enjoined *only* if those assets comprise a readily identifiable *res* which is subject to the ultimate relief of a constructive trust. Lacking such a *res*, the dissent reasoned, Respondent has an adequate remedy at law pursuant to Rule 64 of the Federal Rules of Civil Procedure and Ohio Revised Code § 2715.01, *et. seq.*

The flaw in this argument is that it focuses the determination of the adequacy of legal remedy upon the fortuitous existence of an immediately identifiable *res*, rather than upon the various shortcomings of Ohio's pre-judgment attachment statutes under the circumstances of this case. Indeed, had such a *res* been identifiable, Respondent may have been able to obtain it without the need for equitable relief. It does not logically follow, however, that injunctive relief is only available when it is not needed.

As pointed out by the majority below, Ohio's pre-judgment attachment system:

1. Cannot apply to assets outside Ohio;
2. Requires that securities be garnished by the actual levy upon stock certificates; and,
3. Involves unavoidable delays.

Additionally, under the attachment statutes, the party seeking attachment must submit an affidavit setting forth a description of the property, the location of the property, and the use to which it is being put. Ohio Revised Code § 2715.03(E). Obviously, this could not be accomplished here, where the undisputed evidence revealed a pattern of liquidation and transfer of assets out of Ohio.

Despite Petitioner's argument to the contrary, no decision of this Court precludes or counsels against the preliminary in-

junction herein, and no decision of another Circuit has reached a conflicting determination.

Petitioner has cited several Supreme Court and Circuit Court cases in support of its proposition. *DeBeers Consol. Mines* v. *United States*, 325 U.S. 212 (1945), *Phoenix Mutual Life Ins. Co.* v. *Bailey*, 80 U.S. (13 Wall) 616 (1871), *Adler* v. *Fenton*, 65 U.S. 407 (1861), *Martin* v. *James B. Berry Sons Co., Inc.*, 83 F.2d 857 (1st Cir. 1936), *Wahlgren* v. *Bausch & Lomb Optical Co.*, 77 F.2d 121 (7th Cir. 1935), *Friedling* v. *Freedman*, 44 App. D.C. 191 (1915). However, none of these decision deals, as here, with a claim for an accounting; or with actual as opposed to potential, dissipation of assets; or with a stipulated likelihood of success on the merits; or with the demonstrated inadequacy of state attachment proceedings to effect relief.

Moreover, this Court has recognized that under appropriate circumstances, a district court may enjoin a party from the disposition of property under that party's control. *United States* v. *First National City Bank*, 379 U.S. 378 (1965). Respondent submits that the within circumstances clearly meet the test set forth therein.

The decision below raises no important question of federal law or procedure. It is well established that a district court, sitting in Equity, has broad discretion to apply its injunctive powers. It is likewise clear from the facts herein, that the district court properly responded to a peculiar situation not normally found in routine tort or commercial claims. Indeed, it is the very flexibility of Equity which permitted the district court to fashion the remedy of which Petitioner complains. The promulgation of rigid restrictions upon this flexibility is neither warranted on these facts nor desirable in the abstract.

CONCLUSION

For the reasons set forth above, Respondent, EBSCO Industries, Inc., submits that the Petition for Writ of Certiorari should be denied.

Respectfully submitted,

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